IN

THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No._____

CARNEGIE-ILLINOIS STEEL CORPORATION, a corporation, *Petitioner,*

v.

GEORGE P. ALDERSON, in his official capacity as Tax Commissioner of the State of West Virginia, and in his individual right, *Respondent*

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

For convenience the Carnegie-Illinois Steel Corporation, plaintiff in the Circuit Court, appellant in the Supreme Court of Appeals of West Virginia, and petitioner in the application for writ of certiorari, will be referred to as "plaintiff", and George P. Alderson, in his official capacity as Tax Commissioner of the State of West Virginia, and in his individual right, defendant in the Circuit Court, appellee in the Supreme Court of Appeals of West Virginia, and respondent in this proceeding, will be referred to as "de-

fendant". The transcript of the record presented with the petition for writ of certiorari will be referred to as "Record".

SUMMARY OF ARGUMENT

Plaintiff is lessee from the United States Government of an armor plate factory, including facilities and tools, located upon an exclusive Federal reservation, the lease limiting the use of the premises to the manufacture of products for warships of the United States. It has so-called "lumpsum" contracts with the United States for such product. Because the armor plate factory was only capable of performing certain heat treating processes in the manufacture of armor plate, (it being the only factory owned by the Government) plaintiff and two other private manufacturers whose facilities in the period of national crisis were being used to capacity, alone had the technical organization to operate this factory, and except for such use, its much needed facilities would otherwise not have been available to the Government. West Virginia seeks to impose a privilege tax upon the activities of the plaintiff. It is conceded that the circumstance that the burden of payment of state taxation may ultimately rest upon the United States does not of itself give rise to a nontaxable status, if there be involved only *economic burden,* and such be indirect, of limited extent, and the Government be protected from imposition because of competitive conditions, but all such are essential to a valid state tax, even where fiscal matters of the Government alone are involved. However, a state tax may not impinge, directly or indirectly, upon the exercise of a *sovereign function* of the United States. Such taxation is completely beyond constitutional power of

a state, however slight such impingement may be, and even though private individuals derive profit in furthering the exercise of such sovereign functions. Where activities of a private individual involve use of Government property in furtherance of sovereign functions of the Government, such circumstance renders their activities immune from state taxation.

The activities of the plaintiff, being upon an exclusive Government reservation as to which no concurrent jurisdiction was reserved by the State, are beyond the geographical jurisdiction of West Virginia, particularly as the so-called "Buck Act" (Public No. 819—76th Congress, Chap. 787, 3rd Session) was passed after the status of the plaintiff was established in its relationship with the Government it being contended (a) that said Act properly interpreted does not extend to permitting taxation of the character, and under the circumstances, here present, and (b) in no event will the Act be given retroactive effect in disturbance of a status of contractual relationships prior to its effective date.

ARGUMENT

The most important question in this record is whether or not the activities of plaintiff are inherently immune from State taxation. A question less important in the mind of counsel is whether or not the activities of plaintiff, being on an exclusive Federal reservation, are within the geographical jurisdiction of the State of West Virginia, the so-called Buck Act heretofore referred to having become effective after the establishment of plaintiff's relationships with the Government. In the mind of counsel, properly interpreted,

the Buck Act does not permit taxation of the character and under the circumstances here present and in any event would not be given retroactive effect. However, without in any way waiving petitioner's contention in this particular, counsel will emphasize the more important question only, in this application, because, in the mind of counsel, its far-reaching effect is so obvious that the Court will desire only its presentation upon a preliminary application such as this where the Court's inquiry is only as to the propriety of taking jurisdiction.

It is believed that never in the history of the United States has a state sought to extend its taxing power so far as in the present instance. While it is true that the tax is levied upon a lessee from, and contractee with, the Government, and not, of course, upon the Government itself, nevertheless the ultimate and unquestioned fact is that the State of West Virginia here seeks to impose a tax upon activities in the making of armor plate with Government facilities and tools for warships of the United States at a time of national emergency.

Counsel wishes first to emphasize in the strongest possible way that the situation here presented is absolutely unique, the relationship between the plaintiff and the Federal Government going far beyond a contractual economic relationship. Plaintiff is not merely a contractor with the Government, but is a lessee. Such lease and the resultant activities of plaintiff in using the Government's plant, tools and facilities were absolutely necessary to activate those facilities for the protection of the Nation in a time of crisis. In considering the question as to whether or not the activity of the plaintiff is in the furtherance of the soverign functions of the Government, or springs from a mere economic contractual relationship, it is essential that the exact

nature of the Business-Occupation Tax of West Virginia be borne in mind. There is no question but that it is a pure activity tax. Such has been, and certainly will be, conceded. The demurrer (R. p. 67) correctly speaks of the tax being placed on activity or business. While measured by gross receipts, it is not a tax upon such gross receipts — not a revenue or income tax. Such statement, counsel feel safe in assuming would be agreed to by defendant. Incidentally, if this were a gross income tax, it would be a tax levied on the revenue of a corporation, and as such, under Article 12, Section 4 of the Constitution of West Virginia and the amendment ratified in November, 1902, would be earmarked for the general school fund, and, of course, it is not pretended by the State authorities that all of the proceeds of the Business-Occupation Tax from corporate taxpayers are so destined. Such would dislocate the budget of the State. However, if it be argued that there is only an economic relationship here involved, that the taxable event is receipt of gross income by plaintiff under lump sum contracts, then such receipt would be within Article 12. If, on the other hand, this tax be properly visualized as an activity tax and *the taxable event the activity of the plaintiff,* it follows that the circumstance that it received payments, or makes profit upon its contracts with the Government is immaterial.

The activity here involved, the necessary taxable event, consists of *continued and current activity,* for, and under the supervision of, the United States Government, a wholly different situation both in factual and economic aspects than that presented for example, where a structure such as a dam is built to be ultimately turned over to the Government, or where products or materials are sold to a contractor with the Government.

The conclusion is therefore inescapable, that there is here involved an activity consisting (a) of current manufacturing, (b) for the National Government, (c) using its property, (d) in furtherance of its sovereign functions, and (e) under its supervision. It is believed that such a conclusion may not be questioned, and yet its formulation shows the fallacy of treating the relationship here present as merely one of economic contract.

The question of state power to tax where there is a Federal relationship involved has been the subject of innumerable precedents in the various state and Federal Courts, culminating in a number of decisions by this Court. It is felt that an attempt to analyze, or even to recite, all of them would be an unwarranted trespass upon the time of the Court. After a consideration of a large number of these precedents, with all of the apparent confusion, their shades of reasoning, the niceties of legal and factual distinction, counsel believe that certain general rules are universally recognized and that an analysis of those decisions will disclose the soundness of the following propositions:

(a) It is recognized, particularly under recent decisions of this Court, that the circumstances that the burden of a payment may ultimately fall upon the United States does not of itself give rise to a nontaxable status. If there be involved only an *economic* burden, even if ultimately borne by the United States, and such economic burden be indirect and of limited extent, and the Government be protected from imposition by competitive conditions, a state may have power to tax. Such may be called the "economic burden" rule, and its concept is founded upon the basic distinction between the *economic* and *sovereign* functions of government.

(b) On the other hand, if a tax, either state or Federal, impinge directly or indirectly upon the exercise of a *sovereign function* of the other government, or if sovereign functions be directly or indirectly affected, then such taxation is completely beyond constitutional power.

(c) If the activities of a private party, regardless of whether they relate to economic or sovereign functions of the Federal Government, are so intimately interwoven with the property and activities of the United States that they amount in practical effect to an activity of the United States or its agency, then such activities are beyond the constitutional power of a state to tax.

Counsel believe that the three foregoing doctrines are unquestioned and unquestionable. The difficulty, of course, lies in their application to any particular set of circumstances.

What are the circumstances here present and what rule should be invoked. The contracts were so-called "lump sum" contracts, and if such constituted the only relationship between the United States and this plaintiff, a close question as to taxability might be raised. For example, if this plaintiff had a contract in West Virginia for the manufacture at its own plant (if it had such in the State) for sale to the Government, at a lump sum price, of an article commonly manufactured and sold under competitive conditions, or if it were selling a generally purchasable material such as lumber, cement or the like, or if it were contracting, as the result of competitive bidding, for the building of a structure for the Government, counsel believe it quite possible that the West Virginia Business-Occupation Tax

would be imposable. However, the contracts here rest upon a different basis in that they are for a product that is being sold under noncompetitive conditions, the Government facing an emergency with only three sources from which it may obtain such product, to-wit, this plaintiff, and the two other companies mentioned in the bill of complaint, the South Charleston plant having also been rendered capable of performing certain processes. The facilities of all these three companies (and the South Charleston plant) are unable to meet the emergency. The bill of complaint alleges that future contracts are expected and that if there be a taxable status, it will expect in its cost forecast to add the tax. Under these circumstances, even if lump sum contracts were involved for armor plate from a private mill of the plaintiff, it is the belief of counsel that the lack of competitive conditions, and the consequent substantial and direct burden upon the Government, would render activities under these contracts, standing alone, untaxable. The situation is wholly different than in the case of the purchase of lumber, a common commodity, involved in the *King & Boozer* case later discussed, and in the construction of a dam from easily obtainable materials involved in the *Dravo* case. Whether a state may constitutionally tax transactions and relationship between private parties and the United States turns largely upon the *degree* of that relationship and its circumstances, from the viewpoint of the Government. If there be only an incidental economic burden upon the Government under circumstances where competitive conditions prevent such burden becoming onerous, or if the burden be indirect, there may be such taxation. The importance of competitive conditions was specially stressed in *James* v. *Dravo Contracting Company,* hereafter discussed.

However, the situation is far different from that above postulated. There is very much more involved than merely the question of economic burden upon the Government that would arise under those circumstances. In the unique situation here presented the product in question relates, and is essential, to the exercise of perhaps the most basic and fundamental sovereign power and duty of any nation — the protection and assurance of national safety. On June 8, 1939, the date of the original lease, the armor plate factory had fallen into disrepair. This plaintiff and the two other companies mentioned in the bill of complaint alone had an organization of technical employees capable of performing the highly specialized operations necessary to make plate or to restore this factory to a working condition. The property of the United States, the use of which was so essential to national defense, was worthless without a technical organization such as plaintiff was able to furnish, and none was available to the Government. (Paragraph V and elsewhere, bill of complaint, R. p. 14). The property was to be used solely for the production of armor plate and deck plate for warships built for the United States. There was not a single item of property, or equipment, or a tool that did not belong to the United States, except, of course, in temporary emergencies, before the Government could supply the tools, the Company, on rare occasions, used, temporarily, tools brought from some of its plants out of the State. The plaintiff repaired this dormant plant and made possible the use of most urgently needed facilities of the United States solely for the benefit of the United States, when the plaintiff and two others were the only companies in the whole United States or its dependencies that were capable of so doing. It did so under the most stringent and direct supervision of the

Government, with eight to ten inspectors and with power in the Government, as will appear from the bill of complaint and the exhibited form of contract therewith, that virtually amounted to the Government's officials directing the operations. The practical effect, and, counsel believe, the legal deduction, in this unique situation, is: (a) the activities of the plaintiff were in furtherance of a sovereign function of the government, and (b) plaintiff was, in effect at least, the instrumentality of the United States in making available at a time of crisis the plant, property and tools owned by the government.

With all deference to the learned Supreme Court of Appeals of West Virginia it is respectfully submitted that its conclusion in the official syllabus is erroneous, in that the plaintiff may not be treated as exercising a sovereign function of the Federal Government and therefore exempt from a state tax, in the absence of an Act of Congress recognizing the claimed exercise. (R. p. 74). It is not believed that it was intended by the learned Judge writing the opinion to infer that in order to create an instrumentality of the United States, a specific Act of Congress was necessary. In virtually all of the numerous cases decided by this Court in which private concerns were held to be instrumentalities, or quasi-instrumentalities, of the United States there was no specific declaration of Congress to that effect. There can be no question that the manufacture of armor plate for national protection is a soverign function. It is not a question of the plaintiff exercising such soverign function except as it may do so as an instrumentality, or quasi-instrumentality, of the United States.

What is an instrumentality of the United States?

It is, as it were, a channel, public or private, through which the impulses of Government flow. Here under the allegations of the bill of complaint, of course factually not denied, the Government would have been prevented, at least for a long period, from performing one of its highest functions in the absence of a lease and contracts such as are here present. It is not a question of Congressional designation of plaintiff as an instrumentality. Was it the essential channel through which sovereign activities of the Government were made possible? The allegations here show that it was uniquely so.

With every deference to the learned Court below, it is respectfully urged that there is here no question of a tax *in personam* such as a tax upon a personal net income synthesized from numerous receipts and disbursements over a specific period, or even a gross receipts tax — it is a tax upon an *activity* and in this instance the activity consists of furthering perhaps, the highest sovereign function of National Government.

It will perhaps make for clarity if certain of the cases relied on by demurrant below are analyzed. The principal reliance of the Tax Commissioner and the opinion from which his contention stems that activities of this character are taxable, was *James* v. *Dravo Contracting Co.*, 302 U. S. 184, 82 L. ed. 155, a case under the Act here involved. The activity there in question was the building of a dam in Kanawha River upon land as to which there was concurrency of jurisdiction. The Court on page 166 of the opinion, as reported in Lawyer's Edition, states the issue as to whether or not the tax is invalid, "upon the ground that it lays a direct burden upon the Federal Government". It then

calls attention that the Solicitor General, speaking for the Government, supports the contention of the State that the tax is valid, and further notes that the tax is not laid upon the Government, its property or officers. Here the property of the Government was solely used (with the immaterial exception of temporary use of tools) and plaintiff's activity made that property available to the Government at a time of national crisis. The Court then considers whether the tax under the circumstances there present imposed a direct burden on the Government, saying on page 172 of the opinion as reported in Lawyer's Edition (italics ours):

> "The contention ultimately rests upon the point that the tax increases the cost to the government of the service rendered by the taxpayer. But this is not necessarily so. The contractor, taking into consideration *the state of the competitive market* for the service, may be willing to bear the tax and absorb it in his estimated profit rather than lose the contract."

The decision therefore upheld the validity of the tax, even though its payment might involve an indirect, but not a direct, economic burden upon the Government. The following language appears on page 169 of the opinion, as reported in Lawyer's Edition (italics ours):

> "The question of the taxability of a contractor upon the fruits of his services is closely analogous to that of the taxability of the property of the contractor which is used in performing the services. His earnings flow from his work; his property is employed in securing them. In both cases, the taxes increase the cost of the work and diminish his profits. Many years ago the Court recognized and enforced *the distinction between a tax laid directly upon a government contract*

> *or an instrumentality of the United States and a tax upon the property employed by an agent or contractor in performing services for the United States.* 'Taxation of the agency is *taxation of the means;* taxation of the property of the agent is not always, or generally, *taxation of the means'* ".

The distinction between a mere indirect economic burden and a burden or limitation upon the sovereign activity or efficiency of the Government is preserved throughout the *Dravo* case. Its doctrine may be summarized as follows:

(a) A state may tax the activities of one having a contract with the United States, even though such tax involve an indirect economic burden upon the Government, the Court noting, however, the competitive conditions, which might absorb that burden.

(b) A state may not lay a tax that has the effect of a direct burden on the United States or of limiting its governmental activities.

The *Dravo* case was the first of what may be called the recent "economic burden" decisions. The furthest extension of its doctrine is found in *Alabama* v. *King & Boozer,* 314 U. S. 1, 86 L. ed. 3, with its companion case of *Curry* v. *United States,* 314 U. S. 14, 86 L. ed. 6. There, lumber was purchased by governmental "cost-plus" contractors, the State claiming a sales tax upon the transaction. The Court held that so far as a non-discriminatory sales tax entered into the cost of the materials to the Government, such was a normal incident of the organization within the same territory of two independent taxing sovereignties. The question turned

largely on whether or not such cost-plus contractors were agents of the Government, and it was held that they were not. The Court called attention that it could not be said that the contractors were not, or that the Government was, bound to pay tax on the purchase price of the lumber in question or that the contractors were not the purchasers on whom the statute imposed the tax. Of course, the tax involved in these cases was a so-called consumers' sales tax (and a companion storage or use tax) with an imposition of two per cent upon the sales price of property purchased, a law parallel to our so-called "Consumers Sales Tax." The distinction between a tax on property purchased that was ultimately to be used by the Government and a tax upon a current activity such as that here present, of course, occurs immediately to the mind. It is noted in the opinion of the *King & Boozer* case that the lumber was sold and delivered on the order of the contractors which stipulated that the Government should not be bound, and payment, in fact, was made by the contractors, who were later reimbursed by the Government, when the invoices were approved by its officers. The Court says on page 5 of the *King & Boozer* case, as reported in Lawyer's Edition (italics ours):

> "The contractors were thus purchasers of the lumber within the meaning of the taxing statute, and as such were subject to the tax. They were not relieved of the liability to pay the tax either because the contractors in *a loose and general sense* were acting for the Government in purchasing the lumber or, as the Alabama Supreme Court seems to have thought, because of the economic burden of the tax imposed upon the purchaser would be shifted to the Government by reason of its contract to reimburse the contractors."

The holding in these cases may be summarized to the effect that a sales tax primarily laid with respect of property purchased by a private individual on whom the tax is imposed, is not rendered unconstitutional by reason of the fact that later the individual is reimbursed by the Government and the economic burden of the tax to that extent shifted to the latter.

The case of *Penn Dairies, Inc.* v. *Milk Control Commission of Pennsylvania* 318 U. S. 261, involved the question as to whether or not one who sold milk to the United States to be delivered and consumed by troops stationed at a military encampment on land belonging to the state and occupied under a permit from it which involved no surrender of state jurisdiction, was subject to state regulation as to the milk. As stated in the opinion, the state regulation in question imposed no prohibition on the purchase of milk by the Government from whom it pleased and at what price it could, the Government being affected only as the state's regulation might increase the price of milk generally. Of course, the many distinctions between this case and that here present are apparent. The *Penn Dairies* case at most involved only a typical indirect burden upon the Government, so indirect that before it was inferred there must be two assumptions: (a) The State regulation raised the price of the product generally, and (b) that the Government would pay the increased price. A dealer in milk selling to the Government would be obviously (1) dealing in an easily obtainable product; (2) sustaining only a casual economic relationship with the Government, and (3) wholly removed from dealing with the property of the Government or the exercise of any of its sovereign functions in making that property available for national needs.

These are typical "economic burden" cases, and, of course, nothing in them affects the rule that a state may not, in any way, through taxing powers or otherwise, interfere, burden, or in any manner affect the Government in the exercise of its sovereign functions. On the other hand, immunity in the exercise of its sovereign functions and in the handling of its own property is one of the most zealously guarded of all the prerogatives of the Federal Government. This principle is recognized in the *Dravo* case specifically and in innumerable other precedents. The Court says on page 169 of the *Dravo* case, as reported in Lawyer's Edition, quoting from an earlier decision (italics ours):

> "'It is, therefore, manifest that exemption of Federal agencies from State taxation is dependent, not upon the nature of the agents, or upon the mode of their constitution, or upon the fact that they are agents, *but upon the effect of the tax;* that is, upon the question whether the tax does in truth deprive them of power to serve the government as they were intended to serve it, or does hinder the efficient exercise of their power. A tax upon their property has no such necessary effect. It leaves them free to discharge the duties they have undertaken to perform. *A tax upon their operations is a direct obstruction to the exercise of Federal powers.*'"

What is the line of demarcation between a situation which has the effect merely of indirectly shifting an economic burden to the Government and one which involves some limitation upon its sovereign activities? The question must be determined by the "practical criterion" mentioned by this Court in the *Dravo* case, citing *Willcutts* v. *Dunn,* 282 U. S. 216, 75 L. ed. 304. Incidentally, the latter case is instructive as shown the

approach of the Court in drawing this distinction. There the principle was asserted that a tax upon the obligations (or their interest) of a state or its political subdivisions was not within the constitutional power of the United States because it would affect the borrowing power of the issuer, but gain realized upon the sale of those bonds might be the subject of Federal tax in the absence of a showing that any appreciable burden would thereby be cast on the State's borrowing power.

What is the result of applying the "practical criterion" to the situation as disclosed by the bill of complaint? Under the contract the plaintiff is paid a fixed amount for each ton or pound of product accepted. If the sole question were as to its receipt of profit under a contract made under competitive conditions, counsel could well concede, for the purposes of this argument, that the "economic burden" cases would apply, but it is not a question merely of the receipt of such payment. The bill discloses a situation where any tax with relation to the activities of plaintiff would, under the "practical criterion" standard, limit the Government in the exercise of perhaps its highest sovereign function — the use of its own facilities for defense in time of great national emergency.

Even under the "economic burden" cases, in their furthest extension (and their effect has been clarified by *United States* v. *County of Allegheny,* hereafter discussed), they permit taxation under the limited conditions above set forth when there is involved merely an indirect economic interest in the Government. In no instance do they in any manner permit the State to tax any activities that pertain to the sovereign function of the Government. Where that function is involved

directly or indirectly, immunity from taxation is complete.

The distinction between the *business activities* of the Government and the exercise of a *sovereign function* is drawn most clearly in the case of *Carolina* v. *United States,* 199 U. S. 437, 50 L. ed. 261, a case upholding the right of the United States to exact a license tax upon dealers in intoxicating liquors under the Dispensary Law of that State. The Court says:

> "In order to determine to what extent that implication will go we must turn to the condition of things at the time the constitution was framed. What, in the light of that condition, did the framers of the convention intend should be exempt? Certain is it that modern notions as to the extent to which the functions of a state may be carried had then no hold.
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> "These decisions, while not controlling the question before us, indicate that the thought has been that the exemption of state agencies and instrumentalities from national taxation is limited to those which are of a strictly governmental character, and does not extend to those which are used by the State in the carrying on of an ordinary private business."

In holding that states have no right to impinge in the slightest degree upon the exercise of soverign functions of the Government the courts have been particularly careful where use of Government property is involved. The economic burden cases, so far as counsel has been able to find, and certainly any expressions of this Court, involve the *acquisition* or *construction* of property and materials by the Government, not the *current use* of Government property.

In principle it is submitted that the very recent case of *United States of America* v. *County of Allegheny*, 322 U. S. 174, 88 L. ed. 1209 (commonly known as the *Mesta* case) is pertinent. There the United States had leased to the Mesta Machine Company certain machinery which had been bolted on concrete foundations in Mesta's plant on real property owned by it. The machinery was to be used to manufacture product for the Government but such product, so far as appears from the opinion, and such is necessarily the fact, was not of such unique character as armor plate. The State of Pennsylvania sought to place what amounted to a property tax upon this property, claiming that the taxation was upon the enhancement of land owned by Mesta. The Court ruled in effect that such a tax would be an interference with the Government's use of its property, the Court calling attention:

> "***** If the tax is collected by selling the land out from under the machinery, the effect on its usefulness to the Government would be almost as disastrous as to sell the machinery itself. The coercion of payment from compelling the Government to move its property and interrupt production at the Mesta plant would defeat the purpose of the Government in owning and leasing it."

The court held that the property interests of the Government were not taxable either to it or to its bailee. It is true that the tax there involved was a property tax, but the essence of the opinion is that the Government's use of its property was not to be burdened by a tax, or by being compelled to remove its property if the land upon which it was situated were delinquent in taxes. Not only does the *Mesta Machinery Company* case greatly limit the effects of the so-called "economic bur-

den" cases, but it goes much further in its philosophy of tax immunity than is here necessary to uphold the contention of plaintiff and in principle is controlling of the issue here presented. Throughout the majority opinion, however, it appears that *where an essential use of Government property is involved,* there is an immunity from taxation for the reasons here contended for. The sovereign functions of the Government may not be interfered with in the use of its property, even if such use be by a private individual as the Government's bailee. Here the tax is an activity tax and the activity essentially is the use of the Government's facilities. Such is certainly a more direct interference with the use of Government property and the availability thereof for Government purposes than the property tax which was involved in the *Mesta* case.

Whatever plaintiff receives under its contracts is purely secondary, merely a measure of the tax. Its essential activity is to make such facilities available and usable. All of the tools that are used (with temporary and negligible exceptions as noted in the bill of complaint) belong to the Government. In view of the unique and perculiar situation here presented, it would be immaterial whether the burden of this tax were great or small. The consideration of the extent of the burden of the tax is not essential for a determination of this case because the tax is on the "activity" involved in the use of Government facilities with Government tools upon Government property, and such an activity, contributing directly to the furtherance of the sovereign functions of the United States, is beyond the power of a state to tax, to any degree, directly or indirectly. The principle that the use of property of the Government, or for which it is responsible, is clearly stated in *Choctaw, etc., Railroad Co.* v. *Harrison,* 235 U. S. 292, 59

L. ed. 234, involving a lease of coal mining lands belonging to certain tribes of Indians, the State of Oklahoma seeking to impose a tax upon the gross sales of coal produced under such lease. The agreement of the United States with the Indians, as stated by the Court on page 237 of the opinion (as reported in Lawyer's Edition), imposed upon the Government a definite duty in respect to opening and operating those coal mines. The Court held that *the lessee in such case was the instrumentality* through which such obligation was carried out, the Court saying on page 237 of the opinion as reported in Lawyer's Edition (italics ours):

> "From the foregoing it seems manifest that the agreement with the Indians imposed upon the United States a definite duty in respect to opening and operating the coal mines upon their lands, and *appellant is the instrumentality* through which this obligation is being carried into effect. Such an agency cannot be subjected to an occupation or privilege tax by a state."

Here the facilities and property used are directly owned by the United States and its use is in pursuance of the highest sovereign duty of national defense. It is to be noted in the *Choctaw* case that the lessee of the lands there, just as the lessee of the Government facilities in the present instance, derived gross income and that the tax was measured by such gross income, but such was held immaterial just as it is here immaterial. It is respectfully submitted that the *Choctaw* case is conclusive. It is not cited in the opinion of the West Virginia Supreme Court.

The distinction between a tax upon property whose final use is merely in Government construction and a

tax upon the use of Government property or Government facilities is illustrated in *Trinityfarm Construction Co.* v. *Grosjean,* 291 U. S. 466, 78, L. ed. 918, a case upholding a state excise tax on gasoline consumed by a contractor of the United States in the performance of a contract for the construction of levees. Such tax was upheld and probably there would be no question here that the state, as in the *King & Boozer* and *Curry* cases, could levy a *consumers' tax* upon property purchased by the plaintiff for use in its activities. The Court, however, in the *Trinityfarm Construction Company* case points out the difference between such a tax and the tax status in the *Choctaw* and similar cases, where the use of Government property, or property as to which the Government has an obligation, is concerned. In the latter case the opinion states that constitutional immunity is present, regardless of the amount of the tax. The following language is found on page 920 of the opinion as reported in Lawyer's Edition:

> "Its application does not depend upon the amount of the exaction, the weight of the burden or the extent of the resulting interference with sovereign independence. Where it applies, the principle is an absolute one wholly unaffected by matters or distinctions of degree."

The case of *Johnson* v. *Maryland,* 264 U. S. 51, 65 L. ed. 126, holds, that a state may not require a post office employee to cease driving a Government motor truck in the transportation of mail until he had obtained a license by submitting to an examination before a state official. The basis of the decision is that the operation of a Government facility may not be postponed or affected through a licensing act. The Court says in its opinion:

> "With regard to taxation, no matter how reasonable, or how universal and undiscriminating, the state's inability to interfere has been regarded as established since M'Culloch v. Maryland, 4 Wheat. 316, 4 L. ed. 579. The decision in that case was not put upon any consideration of degree, but upon the entire absence of power on the part of the states to touch, in that way, at least, the instrumentalities of the United States (4 Wheat. 429, 430), and that is the law today."

Of course, the parallel here present with that case is exact. Under the law of West Virginia a payment of the Business-Occupation Tax is for the privilege of engaging in any activity. The tax falls in precisely the same category as a license to operate a motor vehicle, although the measure of the tax is different. The State of West Virginia may not impose a tax as a condition precedent to engaging in the activity of plaintiff in operating and using a Government facility.

It was argued below upon behalf of defendant, however, that plaintiff's contracts were lump sum contracts and the tax was upon the activity in carrying out these contracts, and under the "economic burden" cases the fact that the tax might be added to future contracts and be an indirect burden on the Government was immaterial. We have endeavored to show the fallacy of this argument, particularly under the "practical criterion" rule of the *Dravo* case. Such an argument, furthermore, must fail because the contractual relationship between this plaintiff and the Government is only one part of that relationship. There is involved the making available and using of Government facilities under circumstances where otherwise they could not be made available. If the State, through a pure income tax, had tried to tax the *profit* derived by plaintiff from

such contracts, such might or might not have been sustained under the decisions, but here the tax is an *activity* tax, and the most essential part of such activity is making the Government property available and rendering its use possible in a national crisis.

It is to be emphasized that it is not here a question of whether or not the plaintiff in its actions and activities is corporately and technically an instrumentality of the United States. A private coal mining lessee making a private profit was so held in the *Choctaw* case. The extent to which the courts have gone in holding private corporations instrumentalities of the United States, where their activities are associated with governmental purposes, is illustrated in the many cases recognizing such status in national banks. The latter are private corporations operated for profit, but because they are used by the Government in its financial operations, their activities are universally recognized as beyond the scope of state tax. Their relationship is certainly not so close as that here present where the armor plate factory is a facility directly owned by the Government. In view of the allegations of the bill of complaint taken, as true upon demurrer, as to the experience and technical knowledge required to operate such facility and the restricted character of the corporations having such experience and technical ability, it is wholly immaterial whether or not the plaintiff be regarded as a technical instrumentality of the United States. It may be, as heretofore stated, that the plaintiff, if it were using its own facilities, might under certain circumstances be subject to taxation, but here it is using those of the Government, and when such are used, the personal status of the plaintiff is immaterial. It is likewise immaterial whether the Company derived a profit from the

operation of such facility. The whole doctrine is very well summarized in *Metcalf* v. *Mitchell*, 269 U. S. 514, 70 L. ed. 384, holding that persons employed merely as consulting engineers by states are not officers or employees of the state, the Court drawing the distinction between personally owned property used in dealing with the Government and the immunity extended to an instrumentality itself, which immunity extends to the income derived from it. The Court says:

> "Just what instrumentalities of either a state or the Federal government are exempt from taxation by the other cannot be stated in terms of universal application. But this court has repeatedly held that those agencies through which either government immediately and directly exercises its sovereign powers are immune from the taxing power of the other. Thus, the employment of officers who are agents to administer its laws (Collector v. Day, supra; Dobbins v. Erie County, 16 Pet. 435, 10 L. ed. 1022), its obligations sold to raise public funds (Weston v. Charleston, 2 Pet. 449, 467, 7 L. ed. 481, 487; Pollock v. Farmers' Loan & T. Co., 157 U. S. 429, 585, 586, 39 L. ed. 759, 820, 821, 15 Sup. Ct. Rep. 673), its investments of public funds in the securities of private corporations, for public purposes (United States v. Baltimore & O. R. Co., 17 Wall. 322, 21 L. ed. 597), surety bonds exacted by it in the exercise of its police power (Ambrosini v. United States, 187 U. S. 1, 47 L. ed. 49, 23 Sup. Ct. Rep. 1, 12 Am. Crim. Rep. 699) are all so intimately connected with the necessary functions of government as to fall within the established exemption; *and when the instrumentality is of that character, the immunity extends not only to the instrumentality itself but to income derived from it* (Pollock v. Farmers' Loan & T. Co., and Gillespie v. Oklahoma,

supra), *and forbids an occupation tax imposed on its use* (Choctaw, O. & G. R. Co. v. Harrison, 235 U. S. 292, 59 L. ed. 234, 35 Sup. Ct. Rep. 27; and see Dobbins v. Erie County, Supra).

"When, however, the question is approached from the other end of the scale, it is apparent that not every person who *uses his property* or derives a profit, in his dealings with the government, may clothe himself with immunity from taxation on the theory that either he or his property is an instrumentality of government within the meaning of the rule." (Italics ours)

Of course, the word "instrumentality" is not ordinarily used in the decisions as directly relating to specific property, but a facility of the United States such as an armor plate factory is not only an instrumentality in the broader sense, but, being an actual facility, is *a fortiori,* exempt from state taxation in its use and operation by whatever means or by whatever persons such operation be conducted.

It is to be remembered that the tax involved in the *Choctaw* case was a "gross revenue tax which shall be in addition to the taxes levied and collected upon an *ad valorem* basis", that is, a tax upon gross revenue. Here the tax is directly upon an "activity" merely *measured* by gross revenue. However, in the *Choctaw* case the tax was held invalid. Following the *Choctaw* decision the Court held that the Federal Tax upon *net income* of a state's lessee of school lands could not be upheld, in *Gillespie* v. *Oklahoma,* 256 U. S. 501, 66 L. ed. 338, and later in *Burnett* v. *Coronado Oil & Gas Co.,* 285 U. S. 393, 76 L. ed. 815, held that the Federal *net income tax* could not be upheld upon the income of a lessee from a state. The *Gillespie* case and the

Coronado case were later overruled by *Helvering* v. *Mountain Producers Corp.*, 303 U. S. 386, 82 L. ed. 907. The court did *not* overrule the *Choctaw* case, but distinguished — and, of course, the distinction is clear — between the validity of a net income tax, even though the net income in whole or in part resulted from dealings with the Government, and a direct tax upon the Government's property or interests. The question is stated by the Court on page 913 of the opinion, as reported in Lawyer's Edition:

> "* * * whether in a case where the tax is not laid upon the leases as such, or upon the government's property or interest, but is imposed upon the gains of the lessee, like that laid upon others engaged in similar business enterprises, there is in truth such a direct and substantial interference with the performance of the government's obligation as to require immunity for the lessee's income."

Under this precedent, the plaintiff would probably be required to account to the State of West Virginia for net profits from its business, including that derived from the Government's contracts alleged in the bill, if the State of West Virginia had a corporate net income tax, and such would go to the School Fund under Article XII of the Constitution. Such a tax is predicated upon the *income status* of the individual. It is not directly upon an activity, as in the present instance, involving the use of a Government facility in furtherance of a sovereign function. The *Mountain Producers Corporation* opinion cites the *Choctaw* case, and does not overrule it or in any way limit its doctrine. On the contrary the Court, on page 914 of the opinion, uses the following striking language (italics ours):

> "These decisions in a variety of applications enforce what we deem to be the controlling view — that immunity from non-discriminatory taxation sought by a private person for his property or gains because he is engaged in operations under a government contract or lease cannot be supported by merely theoretical conceptions of interference with the functions of government. *Regard must be had to substance and direct effects.* And where it merely appears that one operating under a government contract or lease is subjected to a tax with respect of his profits on the same basis as others who are engaged in similar businesses, there is no sufficient ground for holding that the effect upon the government is other than indirect and remote."

Here, to repeat the language of the Court, regard must be had to *substance and direct effects.* The allegations of the bill present a unique situation, one in which all of the facilities in the United States to make armor plate are insufficient, and only three corporations, one being plaintiff, have had the experience and the technical training to operate such plants. The operation of the plant in South Charleston is not a matter of business or fiscal activity on the part of the Government, but an essential to the furtherance of perhaps the most important of all governmental functions — the maintenance of national security. There is here no question of a mere shift of economic burden. The State of West Virginia could probably levy a net income tax upon any profits that the plaintiff might make in its dealings with the Government. It could go further, let us assume for the purposes of argument, and levy a tax on the gross proceeds of the contracts that the plaintiff has with the United States, if it were doing work for the government in a competitive field and were using

its own property. However, the Legislature of West Virginia has elected to enact a direct activity tax, and the activity here consists of the operation of a facility and the use of the tools therewith, owned by the United States Government, such operation contributing directly to the sovereign functions of the Government. Under the "practical criterion" test, of course, the tax would act as a "hamper" (to use the phrase of Mr. Justice Holmes) upon the operation of that facility, with only three corporations capable of operating an armor plate plant as alleged in the bill of complaint. The Government could not have the advantage of the competitive conditions which might cause a contractor to absorb the tax, as visualized in the *Dravo* case.

However, the question of any economic burden upon the Government is irrelevant under the authorities. A state has no power to levy a direct tax upon a facility of the government operated in the performance of its sovereign functions, no matter how fair, non-discriminatory or inconsequential such tax might be.

In view of the important aspect of the first question, counsel believes it is unnecessary in this preliminary application to argue the question as to whether or not the Buck Act is operative to best geographical jurisdiction in the State of West Virginia to levy this tax, but such question, of course, is not waived.

CONCLUSION

It is respectfully submitted that this Court in its sound discretion may appropriately grant the writ of certiorari prayed for and that the petition and brief in support thereof present special and important reasons therefor.

Respectfully submitted,

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